

RURAL WATER DISTRICT NO. 3
Osage County, Kansas
Year Ended December 31, 2015

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Rural Water District No. 3
Osage County, Kansas

We have audited the accompanying financial statements of the Rural Water District No. 3, Osage County, Kansas, as of and for the year ended December 31, 2015, which comprise the District's basic financial statements as listed in the table of contents, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the guidance in the Kansas Municipal Audit and Accounting Guide (KMAAG). Those standards and guidance require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error.

Auditor's Responsibility (Continued)

In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Rural Water District No. 3, Osage County, Kansas, as of December 31, 2014, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other-Matters

The District has not presented the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Our audit was conducted for the purpose of forming opinions on the basic financial statements. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in cursive script, reading "Goff & Berry".

January 29, 2016

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF NET POSITION
December 31, 2015

ASSETS

Assets:

Cash and cash equivalents	\$ 290,748
Accounts receivable	7,474
Interest receivable	872
Prepaid insurance	6,007
Inventory	<u>13,470</u>

Total current assets 318,571

Restricted investments:

Revenue bond covenant accounts	59,000
Long-term certificates of deposit	221,655
Note receivable	<u>3,070</u>

283,725

Capital assets:

Property, plant and equipment	2,742,238
Less: accumulated depreciation	<u>1,410,237</u>

1,332,001

Other Assets:

Bond issue costs net of amortization	<u>19,422</u>
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Total assets

\$ 1,953,719

The accompanying notes are an integral part
of these financial statements.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF NET POSITION
December 31, 2015

LIABILITIES AND NET POSITION

Liabilities:		
Current maturities of long-term debt	\$ 80,000	
Accounts payable	24,385	
Accrued payroll	7,049	
Accrued payroll taxes	479	
Accrued interest	1,798	
Other accrued expenses	<u>318</u>	
Total current liabilities		114,029
Long-term liabilities:		
Long-term debt, less current maturities		258,664
Net Position:		
Invested in capital assets, net of related debt	1,012,759	
Restricted for debt service	59,000	
Unrestricted	<u>509,267</u>	
Total net position		<u>1,581,026</u>
Total liabilities and net position		\$ <u>1,953,719</u>

The accompanying notes are an integral part
of these financial statements.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF ACTIVITIES AND
CHANGES IN NET POSITION
Year Ended December 31, 2015

Operating revenues:		
Water sales	\$ 188,395	
Debt service charges	119,544	
Late charges	9,870	
Miscellaneous	<u>8,506</u>	
Total operating revenues		\$ 326,315
Operating expenses:		
Water treatment	22,417	
Depreciation and amortization	58,770	
Wages	78,256	
Payroll taxes	6,071	
Employee benefits	6,871	
Repairs	18,549	
Engineering	-	
Annual water costs	10,579	
Insurance	7,972	
Utilities	20,494	
Mileage	3,880	
Office expense	692	
Postage	2,498	
Dues and subscriptions	412	
Telephone	2,128	
Training	-	
Software	2,000	
Legal	-	
Accounting	5,270	
Miscellaneous	3,231	
Water protection fee	1,376	
Bad debts	<u>31</u>	
Total operating expenses		<u>251,497</u>
Operating income (forward)		\$ <u>74,818</u>

Continued

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF ACTIVITIES AND
CHANGES IN NET POSITION
(Continued)
Year Ended December 31, 2015

Operating income (forward)		\$ 74,818
Non-operating revenue (expense):		
Interest income	3,339	
Interest expense	(5,809)	
Extensions and contributions	(131)	
Loss on sale of equipment	<u>-</u>	
Total nonoperating income		<u>(2,601)</u>
Income before capital contributions		72,217
Capital contributions:		
Benefit units sold - net		<u>-</u>
Change in net position		72,217
Net position, beginning of year		<u>1,508,809</u>
Net position, end of year		<u>\$ 1,581,026</u>

The accompanying notes are an integral part
of these financial statements.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF CASH FLOWS
Year Ended December 31, 2015

Cash flows from operating activities:		
Receipts from customers		\$ 345,914
Payments to suppliers and employees		<u>180,213</u>
Net cash provided by operating activities		165,701
Cash flows from capital related financing activities:		
Principal payments on long-term debt	\$ (80,000)	
Interest paid	(6,142)	
Purchase of capital assets	(77,428)	
Purchase of construction in progress	100	
Benefit units sold	-	
Contributions for construction	(131)	
Restricted investment purchased	<u>(2,097)</u>	
Net cash used in capital and related financing activities		(165,698)
Cash flows from investing activities:		
Principal payments on note receivable	140	
Interest income - CD's and note receivable	3,339	
Sale of equipment	<u>-</u>	
Net cash provided by investing activities		<u>3,479</u>
Net increase (decrease) in cash equivalents		3,482
Cash and cash equivalents, beginning of year		<u>287,266</u>
Cash and cash equivalents, end of year		\$ <u><u>290,748</u></u>

Continued

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

STATEMENT OF CASH FLOWS
(Continued)
Year Ended December 31, 2015

Reconciliation of operating income to net cash
provided by operating activities:

Operating income	\$ 74,818
Adjustment to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	58,770
Changes in assets and liabilities:	
Accounts receivable	19,599
Interest receivable	(227)
Prepaid expenses	1,180
Inventory	-
Accounts payable	11,496
Accrued payroll	17
Accrued payroll taxes	(37)
Other accrued expenses	<u>85</u>

Net cash provided by operating activities \$ 165,701

The accompanying notes are an integral part
of these financial statements.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS

1 - Summary of Significant Accounting Policies

Equity and Basis of Accounting

The District was organized under Kansas law and is accounted for as an enterprise fund using the accrual basis of accounting. The District is not included in any other governmental "reporting entity" as defined in GASB pronouncements, since Board members are elected by the patrons of the District, have decision-making authority, power to designate management, the ability to influence operations and primary accountability for fiscal matters. The District's purpose and objective is to acquire water and water rights, to build and acquire pipe lines and other facilities, and to operate the same for the purpose of furnishing water for domestic, agriculture and for other purposes. The District provides service to patrons in Osage County.

Statement of Cash Flows

For purposes of the statement of cash flows, the District considers all highly liquid investment instruments purchased with an original maturity of three months or less to be cash equivalents.

Investments

Investments represent nonnegotiable certificates of deposit. The certificates of deposit are recorded at cost because they are not affected by market rate changes.

Restricted Investments

Restricted investments represent amounts set aside for the repayment of the Water Utility System Revenue Bonds, Series 2012.

Accounts Receivable

Accounts receivable are carried at original invoice amount less any estimate made for doubtful receivables based on a review of all outstanding amounts. The District reads meters the first day of each month or the earliest day thereafter. Payments for water service are due by the 25th day of the month or will be subject to a 10% late charge. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts.

Management is of the opinion that no allowance for doubtful accounts is necessary.

Inventory

Inventory consists of pipe and parts and is recorded at historical cost.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

1 - Summary of Significant Accounting Policies (Continued)

Capital Assets

Capital assets, which include land, meters and distribution lines, buildings, and equipment, are shown at cost. Depreciation is computed using the straight-line method. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred; significant renewals and betterments are capitalized based on management's judgment. The District has a policy of capitalizing capital assets with a cost greater than \$ 5,000. A deduction is made for retirements resulting from renewals or betterments.

Other Assets

Costs associated with the issuance of bonds are being amortized using the straight-line method over the life of the bond issue.

Capital Contributions

The sales price of benefit unit certificates is considered a contribution to the District. Contributions by developers or patrons for extensions are recorded as patron contributions. Both of these capital contributions are shown on the statement of revenues, expenses and change in net assets.

Net Assets

The District's net assets are classified as follows:

Investment in capital assets, net of related debt - This represents the District's total investment in capital assets, net of accumulated depreciation and related debt.

Restricted for debt service - This represents resources set aside in a bond reserve account in accordance with the bond covenant.

Unrestricted - This includes resources derived from sales and services. These resources are used for transactions relating to providing sales and services and general operations of the District and may be used at the discretion of the governing board to meet current expenses for any purpose.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

1 - Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income Taxes

Rural Water District No. 3, Osage County, Kansas is a tax-exempt entity and not subject to income taxes at either the federal or State level.

Budget

The District is not required to operate under the Kansas Budget laws.

Annual Leave

Under terms of the District's personnel policy, District employees are granted annual leave in varying amounts. At year end, the District estimates that any unpaid vacation pay is immaterial to the financial statements taken as a whole.

2 - Deposits and Investments

At December 31, 2013 and throughout the year ended December 31, 2014, the District's investments included certificates of deposit. As of December 31, 2014, the District had the following investments and related maturities:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Investments Maturities (in Years)</u>			
		<u>Less Than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More Than 10</u>
Certificates of deposit	\$ <u>280,655</u>	\$ <u>-</u>	\$ <u>280,655</u>	\$ <u>-</u>	\$ <u>-</u>

Credit Risk. Kansas statutes authorize the District, with certain restrictions, to deposit or invest in temporary notes, no-fund warrants, open accounts, time deposits, certificates of deposit, repurchase agreements, U.S. Treasury Bills and Notes, the State of Kansas Municipal Investment Pool or to make direct investments. Statues also require the collateral pledged to have a fair market value equal to 100 percent of the deposits and investments, less insured amounts, and to be assigned for the benefit of the District.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

2 - Deposits and Investments (Continued)

Custodial Credit Risk - Deposits. In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a formal policy that addresses custodial credit risk. At December 31, 2015, the District's deposits were not exposed to custodial credit risk.

At December 31, 2015, the carrying amount of the District's deposits, including certificates of deposit, was \$ 570,410 and the bank balance was \$ 570,211, of which \$ 500,000 was covered by federal deposit insurance and the balance was covered by pledged securities with an approximate market value of \$ 128,000 held by the counter party but not in the District's name.

Total deposits and investments of the District are shown in the financial statements as follows at December 31:

	<u>2015</u>
Cash and cash equivalents	\$ 290,748
Restricted investments:	
Revenue bond covenant accounts	59,000
Long-term investments	<u>221,655</u>
	<u>\$ 571,403</u>

3 - Note Receivable

In 1994, the District received a note from Lamont Hill Resort, Inc. To pay the District for providing water to its golf course. The original note balance was \$ 4,705. The term of the note is 35 years with principal and interest paid annually in the amount of \$ 372. The note bears interest at a rate of 7.21%.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

4 - Capital Assets

Capital Assets - Property, Plant and Equipment, together with annual depreciation rates, consisted of the following:

	Estimated Useful Lives	December 31, 2014	Additions	Retirements	December 31, 2015
Capital assets					
Land		\$ 10,556	\$ -	\$ -	\$ 10,556
Meters and distribution lines	10 - 40 yrs	657,459	-	-	657,459
Buildings	15 - 50 yrs	1,904,872	-	-	1,904,872
Office Equipment	3 - 10 yrs	3,395	-	-	3,395
Plant Equipment	5 - 15 yrs	88,528	77,428	-	165,956
Total capital assets		<u>2,664,810</u>	<u>77,428</u>	<u>-</u>	<u>2,742,238</u>
Less: accumulated depreciation for:					
Meters and distribution lines		409,261	8,227	-	417,488
Buildings		904,185	35,546	-	939,731
Office equipment		2,678	394	-	3,072
Plant equipment		41,525	8,421	-	49,946
		<u>1,357,649</u>	<u>52,588</u>	<u>-</u>	<u>1,410,237</u>

5 - Long-Term Debt

Long-term debt consists of the following:

During September 2012, the District issued \$ 590,000 of Water Utility System Revenue Bonds, Series 2012, dated October 1, 2012 to refund the Kansas Rural Water Finance Authority Refunding Revenue Bonds, Series A, 2005 and the Kansas Department of Health and Environment (KDHE) loan. The bonds were dated October 1, 2012, the refunding was undertaken to take advantage of lower interest rates. Net revenue produced from the District's system was pledged as collateral against the bonds. The new bonds bear interest at rates ranging from 1.55% to 1.85%, including principal payments from \$ 80,000 to \$ 90,000 with \$ 5,000 due March 1, 2020, the maturity date.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

5 - Long-Term Debt (Continued)

Annual debt service requirements to maturity for the bonds are as follows:

<u>Year Ending December 31</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Due</u>
2016	\$ 80,000	\$ 5,143	\$ 85,143
2017	85,000	4,083	89,083
2018	85,000	2,765	87,765
2019	90,000	1,341	91,341
2020	<u>5,000</u>	<u>46</u>	<u>5,046</u>
	<u>\$ 345,000</u>	<u>\$ 13,378</u>	<u>\$ 358,378</u>

The following is a detailed listing of the District's long-term debt:

<u>Debt Issue</u>	<u>Date Issued</u>	<u>Original Amount</u>	<u>Interest Rates</u>
Revenue bonds, Series 2012	10-01-12	590,000	1.55 to 1.85%

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

The following is a summary of changes in long-term debt for the year ended December 31, 2015:

<u>Debt Issue</u>	<u>Beginning Principal Outstanding</u>	<u>Additions to Principal</u>	<u>Reductions of Principal</u>	<u>Ending Principal Outstanding</u>
Revenue bonds, Series 2012	\$ <u>425,000</u>	\$ <u>-</u>	\$ <u>80,000</u>	\$ <u>345,000</u>
	\$ <u>425,000</u>	\$ <u>-</u>	\$ <u>80,000</u>	\$ <u>345,000</u>
Less: deferred charge on refunding				<u>6,336</u>
				338,664
Less: current maturities				<u>80,000</u>
				\$ <u>258,664</u>

6 - Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; business interruptions; errors and omissions; employee injuries and illnesses; natural disaster; and employee accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years. There have not been significant reductions in coverage from prior years.

7 - Adequacy of Rates Charged Customers for Services

The District is required to produce revenues sufficient to pay the cost of the operation and maintenance of the system; pay the principal of and interest on the Bonds when they become due and enable the District to have in each fiscal year net revenues, in an amount that will not be less than 125% of the debt service requirements. During 2015, this amount was met at 161%. At December 31, 2015, the District was serving 445 customers.

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

NOTES TO FINANCIAL STATEMENTS
(Continued)

8 - Tax Covenants

The Chairman and Secretary have executed the Federal Tax Certificate in an approved form in order to ensure that the interest on the Series 2012 Bonds will remain excluded from federal gross income.

9 - Subsequent Events

Management has reviewed subsequent events through January 29, 2016.

SUPPLEMENTARY INFORMATION

RURAL WATER DISTRICT NO. 3
Osage County, Kansas

INSURANCE COVERAGE
December 31, 2015

The District's insurance policy is provided by EMC Insurance Companies, with a premium of \$ 12,823 and covers the period June 20, 2015 to June 20, 2016, it provides the following coverage:

Building and personal property (Deductible \$1,000, earthquake deductible of 10% applies)	\$	4,415,070
General liability		500,000
Products completed operations aggregate limit		1,000,000
Personal and advertising injury limit		500/500,000
Damage to premises rented		100,000
Medical expense limit		5,000
Public officials liability each wrongful act (Deductible \$ 1,000 per claim)	1,000,000/1,000,000	1,000,000
Auto liability (non-owned vehicles)		100,000
Employee theft - per loss (Deductible \$ 1,000 per occurrence)	1,000,000/1,000,000	Statutory
Commercial excess liability		500,000
Worker's compensation		
Employer's liability		